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THE SEPARATE ESTATES OF NON-BANKRUPT PARTNERS IN THE BANKRUPTCY OF A PARTNERSHIP UNDER THE BANKRUPT ACT OF 1898.[1]

Dedicated to Professor Langdell.

THE federal courts have almost unanimously held that under the Bankrupt Act of 1898 a partnership is to be treated as an entity. This is something wholly new. Under all prior acts, English and American, a partnership could be put into bankruptcy only by adjudicating all its members bankrupts. Courts of equity and bankruptcy courts have indeed often been driven by the necessity of the case to deal with the firm as an entity, and they have also frequently described the firm as an entity.[2] The same court that declares that the firm as an entity cannot be adjudged bankrupt unless all the partners are bankrupt, will, after the adjudication of its partners as bankrupt, proceed to decide questions on the theory that the firm is a legal person. But as courts of law are not consistent in denying the personality of the firm, so courts of equity are not consistent in admitting it. The very same court will at one time deal with the firm as a person, and at another time

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1 In the notes upon the law of Continental countries the *société en nom collectif* or *Offene Handelsgesellschaft* is taken as the equivalent of the English and American partnership or firm. The *société en commandite* or *Kommanditgesellschaft*, the counterpart of our limited partnership, is for the most part subject to the same rules as the *société en nom collectif* except as regards the special partners (*commanditaires* or *Kommanditisten*), who risk only their subscribed capital.

2 See for a collection of cases an admirable article on The Firm as a Legal Person, 57 Cent. L. J. 343.

assert that it is not an entity. So far, however, as concerns the question of adjudging the firm bankrupt as a firm, there has been no difference of opinion. In the case of *In re* Beauchamp Brothers[1] Lord Esher said, "You cannot adjudicate the abstract thing called 'a firm' bankrupt. You cannot make a firm bankrupt unless you can make the members of the firm bankrupt." It was, therefore, not surprising that with all the authority, statutory and judicial, to the contrary, the first court that had occasion to consider the question of the nature of a partnership under the Bankrupt Act of 1898 should have been somewhat puzzled.[2] Section 5 *a* of that Act provides that "a partnership during the continuation of the partnership business, or after its dissolution, and before the final settlement thereof, may be adjudged a bankrupt." Section 1 (19) provides that "'persons' shall include corporations, except where otherwise specified, and officers, partnerships," etc. With some hesitation the court held that these two sections authorized the adjudication as bankrupts of a firm and one of its members who had committed an act of bankruptcy, which was also an act of bankruptcy of the firm, although the other member could not be adjudged a bankrupt because he had committed no act of bankruptcy. The Circuit Court of Appeals affirmed this judgment,[3] and the precedent thus set has been followed in all jurisdictions but one, to be hereafter mentioned.

This construction of the Bankrupt Act naturally led to decisions that the firm might be adjudged bankrupt when no partner was or could be made a bankrupt,[4] and also that all the partners might be adjudged bankrupt without adjudging the firm a bankrupt.[5] But the District Court of Massachusetts has found insuperable obstacles in the way of construing the Act so as to deal with the firm as an entity.[6] This court had found no difficulty in holding that where one of the partners is a minor, an adjudication can be made against the adult partner and against the firm.[7] But where one partner filed a petition to bring the firm and his co-partner into bankruptcy, it was held that the co-partner might set up the

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1 [1894] 1 Q. B. 1, 5.

2 Chemical Bank *v.* Meyer, 92 Fed. Rep. 896.

3 *In re* Meyer, 98 Fed. Rep. 976.

4 *In re* Stokes, 106 Fed. Rep. 312; *In re* Meyer, 98 Fed. Rep. 976, 979 (*semble*).

5 *In re* Mercur, 116 Fed. Rep. 655; s. c. 122 Fed. Rep. 384; Ludowici Roofing Co *v.* Penn. Institute, 116 Fed. Rep. 661.

6 *In re* Forbes, 128 Fed. Rep. 137.

7 *In re* Dunnigan, 95 Fed. Rep. 428.

defense that he was solvent, because an adjudication against all the partners, it was said, is essential to one against the firm, and that on the issue of solvency the co-partner is entitled to a trial by jury. The court arrived at the result by finding that certain parts of Section 5 other than those already quoted were not reconcilable with the theory of an entity. It must be admitted that all the provisions of Section 5 are not wholly consistent with the idea of the firm as an entity. Clause *h* of Section 5[1] is somewhat ambiguous.

The District Court of Massachusetts arrives at one conclusion as to its effect upon the present question, while the District Court of the Eastern District of Pennsylvania,[2] and the Circuit Court of Appeals of the Third Circuit affirming the judgment,[3] reach the opposite conclusion. Some other clauses of the section were also relied upon by the District Court of Massachusetts, which do not seem to the writer, however, to stand in the way of holding that Congress intended to treat the firm as an entity for the purposes of bankruptcy. But the possibility of finding such apparent contradictions between different clauses of the section, as well as the re-enactment by Section 5 *f* of the old rule of distribution of the partnership and individual estates, indicates that the scheme of treatment of partnerships in bankruptcy was not fully thought out by the draftsman to its logical conclusion. The theory was a new thing, and the changes necessary to the application of the theory seem not to have been carefully considered. Liberality of construction would, however, seem to be desirable and to lead to approval of the result reached by the great majority of the federal courts.

But it is not the purpose of this article to discuss the question upon which the indicated difference of opinion has arisen, but assuming the firm to be an entity under the Bankrupt Act to consider the question of the treatment of the firm and individual estates where the firm alone has been made a bankrupt. The rule of distribution both in England and in America when all the partners are in bankruptcy, greatly criticized by the courts but

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1 "In the event of one or more, but not all of the members of a partnership being adjudged bankrupt, the partnership property shall not be administered in bankruptcy unless by the consent of the partner, or partners, not adjudged bankrupt; but said partner, or partners, not adjudged bankrupt, shall settle the partnership business as expeditiously as its nature will permit, and account for the interest of the partner, or partners, adjudged bankrupt."

2 *In re* Mercur, 116 Fed. Rep. 655.

3 *In re* Mercur, 122 Fed. Rep. 384.

grudgingly yielded to, apparently more to save trouble than for any other reason,[1] may be made to run like some jingle, "firm estate to firm creditors, separate estate to separate creditors, anything left over from either goes to the other." It is believed that this rule is to be found in no other country,[2] and it is to be regretted that Congress did not avail itself of the opportunity to enact a rule of distribution more scientific and more in accordance with the principle of partnership liability, whether the firm be regarded as an entity or not.[3]

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[1] Thus does Sir Frederick Pollock paraphrase the language of Lord Blackburn in Read *v.* Bailey, 3 App. Cas. 102. Pollock, Partnership, 8 ed., 155, n. 4.

[2] In France, although the codes make no express provision, the majority opinion is that the firm creditors take the firm estate and compete with the separate creditors upon the separate estate for any unpaid portion of their claims. Troplong, Droit Civ. Contr. de Société, t. 2, nos 857–863; Sirey et Gilbert, Codes Annotés, Art. 1864, nos 18, 19; Sirey, Code de Commerce, Art. 18–19, nos 128, 129; Fremery, Études de Droit Commercial, 32–33, 372; Lyon-Caen et Renault, Droit Commercial, t. 8, no 1190.

In Switzerland the Code Fédéral des Obligations, Art. 566, in express terms gives the firm estate to the firm creditors to the exclusion of the separate creditors, and Art. 568 permits the firm creditors to pursue the separate estate for any unpaid balance in competition with the separate creditors, if the firm estate is insufficient to pay the firm creditors in full.

In Scotland the firm creditors rank in full on the firm estate, to the exclusion of the separate creditors, and rank on the separate estates *pari passu* with the separate creditors for the unpaid balance. 2 Clark, Partnership, 753.

In Germany, Art. 733 of the Civil Code (Bürgerlichesgesetzbuch) devotes the firm property to the payment of firm debts, and Art. 212 of the Bankruptcy Law (Konkursordnung) permits the firm creditors to seek satisfaction from a partner's separate estate in bankruptcy *pari passu* with his separate creditors for any balance not paid by the firm estate in bankruptcy. Sarwey-Bossert, Konkursordnung, Vierte Auflage, 496–497. It is contended by Kohler, Leitfaden deutschen Konkursrechts, Zweite Auflage, 198–199, that the firm creditor may prove the full amount of his claim against the individual estate, receiving, however, of course, dividends only to the amount of the unpaid balance; but this view is not generally adopted (Sarwey-Bossert, 497, n. 3 b).

In Austria the firm creditor may prove the full amount of his claim against the separate estate. Konkursordnung, § 201; Handelsgesetzbuch, § 31; Kissling, Oesterreichische Konkursordnung, 295–296.

In Hungary the firm creditors are paid first from the firm assets, and come upon the separate estate for the deficiency. Code de Commerce, Art. 97; Loi sur la Faillite, Art. 251 (French translation by De la Grasserie).

[3] In France it is almost universally agreed that a partnership is an entity, *une personne morale, un être moral.* Lyon-Caen et Renault, Droit Commercial, t. 2, nos 105–124. And the personality of the firm is expressly admitted in the Belgian Loi sur les Sociétés of May 18, 1873, Art. 2, where, after enumerating five kinds of commercial *sociétés*, one of which is the ordinary partnership, it is provided that "*chacune d'elles constitue une individualité juridique distincte de celle des associés.*"

The Commercial Codes of Italy, Art. 77 (French translation by Turrel), and of Roumania, Art. 78 (French translation by Bohl), read, "*À l'égard des tiers, les sociétés sus-énoncées sont des êtres collectifs distincts de la personne des associés.*" And the Com-

Our rule of distribution is totally at variance with the mercantile view of partnership.[1] But even upon the legal theory it cannot be justified. To give the firm estate to the firm creditors to the exclusion of the separate creditors is of itself a personification of the firm, since otherwise the property would simply belong to the members as joint tenants or tenants in common, and so be subject to the claims of their individual creditors as fully as any other property of the members.[2] And on the other hand, if the firm is but an association of individuals, the creditors of the firm are creditors on the joint obligations of those members, and as such have the same rights against the property of each member, including therein property held by them jointly with others, as have his individual creditors. If the rule which throws the firm creditors first upon the firm estate is put upon the ground that the firm is the principal and the members are sureties, this too is a recognition of the firm as a different person from the members. If the principle of marshalling be invoked to justify the rule of distribution, it is to be observed that the application of this principle is only conceivable on the assumption that the firm creditors have a right to resort to a fund which the individual creditors cannot

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mercial Code of Spain, Art. 116 (French translation by Prudhomme), provides that "*La société commerciale une fois constituée possédera la personnalité juridique pour tous ses acts et contrats.*"

In Scotland the firm "constitutes a *quasi persona* of which the members are agents and sureties — a principle which exactly realizes the notion of a firm entertained by mercantile men both in this country and in England" (1 Clark, Partnership, 31), and it may therefore be rendered bankrupt without any of its partners being either bankrupt or insolvent. 2 *ibid.* 750.

In Russia the Commercial Code makes no provision on the subject, but it is said that Russian jurisprudence recognizes the personality of the firm. Code de Commerce Russe, 20–21 (French translation by Tchernow).

In Louisiana the partnership is an entity, "a moral being distinct from the persons who compose it"; "a civil person which has its peculiar rights and attributes." Smith *v.* McMicken, 3 La. Ann. 319, 322; Succession of Pilcher, 39 *ibid.* 362; Rivers *v.* City, 42 *ibid.* 1196; Wolfe *v.* Pants Co., 52 *ibid.* 1357; Newman *v.* Eldridge, 107 La. 315.

In Germany, although the partnership can in its firm name acquire rights and contract obligations, acquire property and other real rights in immovables, can sue and be sued (Handelsgesetzbuch, Art. 124), and although, as we have seen, the firm property is specially devoted to the firm creditors to the exclusion of the separate creditors until the firm creditors are paid in full, yet, the codes making no express provision on the point, the question whether a firm is a legal person has been the subject of much discussion and difference of opinion. Lyon-Caen et Renault, Droit Commercial, t. 2, 100; 1 Behrends, Handelsrecht, § 62, n. 2.

[1] Corey, Accounts, 2 ed., 124; Ames, Cas. on Partnership, 367, n. 1.

[2] Lyon-Caen et Renault, Droit Commercial, t. 2, 87.

reach, — an assumption which involves a recognition of the entity of the firm; and even if the assumption is made, the principle is not consistently applied. It is true that the rule of marshalling would oblige the firm creditors first to exhaust the estate against which the separate creditors had no claim, but after the exhaustion of the firm estate the rule of marshalling would permit the firm creditors to come against the separate estates *pari passu* with the separate creditors. Nevertheless, the old rule of distribution has been re-enacted by Congress in Section 5 *f* of the Bankrupt Act of 1898, and must be taken into account in considering the question under discussion; — namely, how is the court which has adjudicated a firm bankrupt, but not the individual partners, or less than all of them, to reach the property of the non-bankrupt partners?

There is a difference of opinion in Continental countries upon the question whether the bankruptcy of the firm necessitates the bankruptcy of the partners.[1] Where the question has been answered in the affirmative the property both of the firm and of the individual members comes into the hands of a bankruptcy court or courts for distribution, but no European jurisdiction has been found where, the firm alone or the firm and some only of the partners being bankrupt, the court has undertaken to seize and administer the property of the non-bankrupt partners. But in the case of *In re* Meyer,[2] the court, speaking of Section 5 of the Bankrupt Act of 1898, said that, "it is the scheme of these provisions to treat the partnership as an entity which may be adjudged a bankrupt by volun-

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[1] In France it is generally held, although not without opposition, that the bankruptcy of the firm involves (*entraine*) the bankruptcy of the partners. Lyon-Caen et Renault, Droit Commercial, t. 8, n[os] 1144–1148. Sirey, Code de Commerce, 3 ed., 469, n[o] 65. The argument is that, as the Commercial Code provides (Art. 437) that every trader who ceases his payments is in a state of bankruptcy, the cessation of payments by the firm necessarily implies cessation of payments by the partners who are personally liable for the debts of the firm (all the partners in the *sociétés en nom collectif* and the general partners in the *sociétés en commandite*).

The Commercial Codes of Italy (Art. 847), Spain (Art. 923), Portugal (Art. 746), Roumania (Art. 860), and the Konkursordnung of Austria (Art. 199), expressly provide that the bankruptcy of the firm shall entail the bankruptcy of the members who are subject to unlimited liability for the debts. Some of the codes further provide that the bankruptcy of the firm and of its members shall be declared by the same judgment (Italy, Art. 847; Roumania, Art. 860; Portugal, Art. 746; Austria, Art. 199). In Germany, however (Sarwey-Bossert, Konkursordnung, 496, n. 1; 1 Behrend, Handelsrecht, 589), and in Switzerland (Code Fédéral des Obligations, Art. 573), the law is contrary to that of the jurisdictions above enumerated, and the bankruptcy of the firm does not necessarily draw with it the bankruptcy of the members.

[2] 98 Fed. Rep. 976, 979.

tary or involuntary proceedings, irrespective of any adjudication of the individual partners as bankrupt, and upon an adjudication to draw to the administration the individual estates of the partners as well as the partnership estates, and marshal and distribute them according to equity." Relying upon this dictum, the court in *In re* Stokes,[1] when the firm alone had been adjudged bankrupt and each of the two partners had previously made an assignment of his individual estate for the benefit of creditors, made a summary order upon the assignees of the non-bankrupt partners to transfer the individual property in their hands to the trustee in bankruptcy. Again, in Dickas *v.* Barnes,[2] the firm had committed an act of bankruptcy by making an assignment for the benefit of its creditors. Some of the partners had participated in making the assignment, and some of them had made individual assignments. Some of the members were adjudged bankrupt, as was also the firm. Some of the members were not adjudged bankrupt, two because they had not committed any act of bankruptcy, and two because they were not subject to involuntary bankruptcy — one being a wage-earner and the other a tiller of the soil. The court ordered all the partners, whether adjudged bankrupts or not, to file schedules of their debts and inventories of their property, and to turn over all their property to the trustee in bankruptcy to be administered as if each of them had been adjudged bankrupts.

The orders in these two cases seem high-handed, and to be defended, if at all, only on the ground of necessity. Is such an order necessary for the protection of the firm creditors, with whom alone the court would seem to be concerned in the bankruptcy of the firm? A firm creditor's interest in the property of the non-bankrupt partner is simply that it may be subjected to the payment of his claim, and this end can be attained by an action against the non-bankrupt partner, who can interpose no defense on the ground that the firm is in bankruptcy. In the converse case of the bankruptcy of a partner without the firm being bankrupt, the Act provides that unless the other partners consent, the firm property shall not be administered in bankruptcy, but that the non-bankrupt partners shall settle the partnership business and account for the interest of the bankrupt partner.[3] There is nothing here to

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1 106 Fed. Rep. 312.

2 140 Fed. Rep. 849.

3 Bankr. Act of 1898, § 5 *h*.

prevent a firm creditor in such a case from suing the non-bankrupt partners, and if the justice of the claim were denied it would indeed be their duty to contest it. Nor is there anything in the Act to prevent a firm creditor from suing a non-bankrupt partner when the firm alone is adjudged bankrupt.[1] Still less than the interest of the firm creditor, does the interest of the individual creditor of the non-bankrupt partner require such orders as were made in the two cases above mentioned. It is certainly to the interest of the individual creditor that he should be left perfectly free to enforce his claim against his debtor's property by action, attachment, and execution. It therefore appears that the summary order really hinders both the firm creditors and the individual creditor from prosecuting their rights against their debtor who is not a bankrupt.

It is to be remembered that the nature of the liability of the members of a firm continues to be the same, although the Bankrupt Act provides for the bankruptcy of the firm as an entity; — that is, a liability directly to the firm creditors. Even in countries where the firm is recognized as an entity for all purposes, it is the general rule that the partners are liable *in solido*,[2] although in most of these countries the enforcement of the liability is de-

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[1] The bankruptcy court could not stay these actions under § 11 *a* of the Act. That section reads as follows: "A suit which is founded upon a claim from which a discharge would be a release, and which is pending against a person at the time of the filing of a petition against him, shall be stayed until after an adjudication or the dismissal of the petition; if such person is adjudged a bankrupt, such action may be further stayed until twelve months after the date of such adjudication, or if within that time such person applies for a discharge, then until the question of such discharge is determined." This section relates only to suits against persons against whom a petition in bankruptcy has been filed, and in respect to a claim which will be released by a discharge, and is evidently inapplicable to persons who have been found not to be subject to the bankruptcy laws, whether because they have committed no act of bankruptcy or because they have been excepted from its operation. Where an action was brought in a state court against two partners and one of them was afterwards adjudged a bankrupt, he was held to be entitled to a continuance of the action until the question of his discharge should be determined. But a motion by the other partner for a continuance was denied and the action proceeded against him. Hogendobler *v.* Lyon, 12 Kan. 276. Under a provision of the English Bankruptcy Act, similar to Act of 1898, § 11 *a*, above quoted, it was held that when a firm creditor had sued the partnership and had attached its goods, and one of the partners afterwards filed a petition for liquidation under the Bankruptcy Act, the court had no jurisdiction to restrain the action. *Ex parte* Isaac, L. R. 6 Ch. 58.

[2] See Codes de Commerce, France, Art. 22; Italy, Art. 106; Spain, Art. 127; Hungary, Art. 88; Roumania, Art. 106; Portugal, Art. 105, 153; Switzerland, Art. 544; Russia, Art. 77; Belgium, Loi du 18 Mai 1873, Art. 17; Germany, Art. 128; Holland, Art. 18.

pendent upon certain preliminary proceedings against the firm.[1] Yet where the bankruptcy of the firm does not necessarily involve the bankruptcy of the members of the firm, we find no country in which such a course of procedure is followed as that adopted in the cases under discussion.

In Germany the partners are personally liable to creditors for the debts of the firm.[2] But although an independent bankruptcy proceeding can be instituted against the firm property,[3] yet the bankruptcy of the firm does not involve the bankruptcy of the partner. By Article 122 of the former Handelsgesetzbuch, the firm creditors in case of the bankruptcy of the firm could have recourse against the individual property of the partners only for what remained unpaid after application of the firm property to their claims. This limitation was applicable not only when the partner was in bankruptcy, but also when he was not, thus preventing the firm creditors from pursuing a non-bankrupt partner pending the ascertainment of the deficiency in firm assets. Article 122 was not re-enacted in the new Handelsgesetzbuch, but by Article 212 of the Konkursordnung it was provided that in case a partner was

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[1] In Italy, Art. 106, the firm creditor must exhaust his action against the firm before he can sue the partners. So in Roumania, Art. 106, and in Portugal, Art. 153. In Switzerland, Art. 564, the partners can be called upon for payment of firm debts only after dissolution, or after the firm has been unsuccessfully pursued. In Spain, Art. 237, the separate property of a partner cannot be seized for a firm debt until after seizure of the firm property. In Belgium, Loi du Mai 1873, Art. 122, no judgment can be rendered against the partners until after judgment against the firm. In Scotland the debt must first be "constituted" against the firm, and it can then "be enforced against the members as guarantees bound conjunctly and severally with their principal"; as soon as the debt is constituted against the firm, execution is competent against any one of the partners. 1 Clark, Partnership, 285, 627.

In France, according to some authorities, the partner can be sued personally only after judgment against the firm, according to others, only after exhaustion of the firm assets, and according to others, after a demand made in certain ways. Sirey, Code de Commerce, 3 ed. 38, n° 52; Lyon-Caen et Renault, Droit Commercial, t. 2, n° 281. In Louisiana, although the ultimate liability of the partners is *in solido*, during the life of the partnership they cannot be charged individually, except through the partnership, which alone can be sued for a partnership debt. Liverpool, etc., Nav. Co. *v.* Agar, 14 Fed. Rep. 615. In Germany, however, no preliminary steps against the firm are necessary before action against the partners. Handelsgesetzbuch, Art. 128, 129; 1 Behrend, Handelsrecht, § 73. The creditor may sue the firm and then the partners, or the firm and partners at the same time, separately or in the same action, or only the partners or any one of them. A judgment against the firm alone cannot be enforced against the individual partners, but they must in such case be sued separately. 1 Lehmann-Ring, Handelsgesetzbuch, 277, Nr. 10; Handelsgesetzbuch, Art. 129.

[2] Handelsgesetzbuch, Art. 128.

[3] Konkursordnung, Art. 209.

adjudged a bankrupt, then the firm creditor could seek satisfaction from the separate estate of the bankrupt partner only for what he had failed to get from the partnership estate. As the law of Germany now stands, where only the firm is in bankruptcy the creditors of the firm are deprived of no rights against the individual partners, but may sue them and proceed to judgment and execution against the private property just as before the bankruptcy of the firm.[1]

Although differing in some respects, the German law of partnership more closely resembles our law than that of any other country examined. In Germany, as in this country, the partners are personally liable to the full extent, and no preliminary proceedings against the firm as such are necessary to establish the liability of the partners. As in many of our states, the partnership may sue and be sued in the firm name. In Germany the firm can be declared bankrupt without any of the partners being made bankrupt, and *vice versa*. Since the passage of the Bankrupt Act of 1898, this is also our law. But in Germany the bankruptcy of the firm alone has no effect upon the separate property of the partners. It is not seized and administered in the firm bankruptcy,[2] nor is even the property of another partnership composed of the same members. Unless the individual partner is put into separate bankruptcy his property remains in his hands and is subject to direct attacks by his creditors, both firm and individual. This seems the logical result of a law which makes partners individually liable and at the same time provides for the bankruptcy of the firm apart from the bankruptcy of its members. A law under which the bankruptcy of the firm draws after it the bankruptcy of the members and so brings both firm and separate estates to be administered at the same time, is comprehensible, but, in a jurisdiction where the bankruptcy of the firm does not entail that of the partners, it seems illogical for the court administering the estate of a bankrupt firm to seize or order the surrender of the property of the non-bankrupt partners. The business of the bankruptcy court is to distribute the property of bankrupt debtors, which property may consist of real estate and personal property, including choses in action. But for the court to have

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1 Lehmann-Ring, Handelsgesetzbuch, 313, Nr. 5; Sarwey-Bossert, Konkursordnung, 497, Nr. 2.

2 Lehmann-Ring, Handelsgesetzbuch, 312, Nr. 2; 280, Nr. 6; Burchardt, Feststellung im Konkurse, 86, 87.

jurisdiction to deal with property it must belong to the bankrupt. It can get possession of the tangible property of the bankrupt by summary order on those holding it, but it cannot reduce a chose in action to possession by a summary order on the bankrupt's debtor commanding him to turn over enough property to pay it. The trustee must sue to collect the debt. By the summary order in the cases discussed the court does not take possession of any property belonging to the bankrupt, for the property of the non-bankrupt partner does not belong to the firm. The summary order upheld by the Supreme Court in Mueller *v.* Nugent[1] was directed to those who, without honest claim or right, withheld property of the bankrupt, not property which it was conceded belonged to the person holding it.[2]

It is true that it is also the business of the court to pay the debts of the bankrupt, but how? With the property of the bankrupt, not with the property of third persons. The fact that the debts of the firm are also debts of the non-bankrupt partners should no more give the court power over the property of the non-bankrupt partner than the bankruptcy of one of two joint debtors should authorize the court to seize the property of the non-bankrupt joint debtor. If the bankrupt's trustee has paid more than the bankrupt's share of the debt, he may, no doubt, sue the non-bankrupt joint debtor for contribution, but the court of bankruptcy would never order the non-bankrupt to turn over his property to the trustee either before or after such payment by the trustee.

In the case of *In re* Beauchamp,[3] Kay, L. J., said, "A receiving order is only to be made as a step towards an adjudication of bankruptcy, and when you cannot have an adjudication of bankruptcy, it seems to me that you ought not to obtain a receiving order. To allow this receiving order to stand would be in effect to put in

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1 184 U. S. 1.

2 See also the case of Louisville Trust Co. *v.* Comingor, 184 U. S. 18, in which it was held that the court cannot by a summary order compel the payment to the trustee of money which is claimed to be the lawful property of the person against whom the order is directed. When the fact of an honest claim appears, the court can go no further under the order, but must leave the trustee to pursue his remedy in the customary mode of proceeding in the proper court. Nor was the case made any better for the trustee by reason of the fact that the person withholding the money had been made a party to the petition in bankruptcy, although no cause of action was set up and no special relief was prayed against him. See also Jaquith *v.* Rowley, 188 U. S. 620; *In re* Michie, 116 Fed. Rep. 749.

3 [1894] 1 Q. B. 1, 8.

the power of the official receiver the property of a person who could not be made a bankrupt, who has not committed an act of bankruptcy, and who is not subject to the bankruptcy laws. I think, therefore, that the receiving order is a bad one, and we must simply set it aside." The House of Lords cut the knot in that case by holding that a receiving order could be made against the firm "other than" the partner who could not be made a bankrupt.[1]

In that case, it is true, the partner who could not be made a bankrupt was an infant, but the language of Kay, L. J., above quoted, shows that he would disapprove of any order which put into the hands of the trustee in bankruptcy "the property of a person who has not committed an act of bankruptcy and who is not subject to the bankruptcy laws," whatever might be the reason for such exemption.

With all deference to the learned court which decided the case of Dickas *v.* Barnes,[2] the ruling in that case seems nothing short of judicial legislation. The court sustained orders requiring persons who had committed no act of bankruptcy and persons who, being wage-earners or tillers of the soil, could not be adjudged involuntary bankrupts, to file schedules of debts and inventories of property, and to hand over all their property to the trustee of the firm in bankruptcy. We find nothing in the Bankrupt Act to justify these orders. The Act imposes the duty of filing a schedule of property and a list of creditors only upon a bankrupt;[3] and the duties of the referee to examine schedules of property and lists of creditors and to prepare and file them when the bankrupts fail, refuse, or neglect to do so, relate only to those filed, or which ought to be filed, by bankrupts.[4] Nor do we find anything in the section of the Act which defines the jurisdiction of the courts of bankruptcy.[5]

The only clauses of that section relevant to this question are clauses (7)[6] and (15).[7] Clause (7) clearly confers no jurisdiction to collect and distribute the estate of a non-bankrupt. Nor can

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[1] Lovell *v.* Beauchamp, [1894] A. C. 607.

[2] 140 Fed. Rep. 849, *supra*, p. 595.

[3] Bankr. Act of 1898, § 7 (8).

[4] *Ibid.*, §§ 39 (2), 39 (6).

[5] *Ibid.*, § 2.

[6] "Cause the estates of bankrupts to be collected, reduced to money and distributed, and determine controversies in relation thereto, except as herein otherwise provided."

[7] "Make such orders, issue such process and enter such judgments in addition to those specifically provided for, as may be necessary for the enforcement of the provisions of this Act."

clause (15) be invoked. Such an order as the one under discussion cannot be necessary for the enforcement of any provisions of the Act. The order aimed to bring into the hands of the trustee property which the court had no jurisdiction to collect and distribute, because by clause (7) it was only estates of bankrupts which were to be so dealt with. In the case of Louisville Trust Co. *v.* Comingor,[1] the property in question was claimed to be the property of the bankrupt. Yet even in that case jurisdiction to issue a summary order to compel the possessor to turn the property over to the trustee, was denied merely because the possessor made an honest claim of rightful ownership, while in the case under consideration the property is confessedly not that of the bankrupt.

The learned court which sustained the orders in Dickas *v.* Barnes admitted that the orders could not ordinarily have been made against persons not subject to the Bankrupt Act, but the court thought that the rule must be otherwise where the non-bankrupts were partners in a bankrupt firm. The reason given was that "one who combines with others in a partnership enterprise becomes bound for the payment of the partnership debts. As partner he shares the fortunes of the partnership. In certain circumstances it may become subject to the exercise of the powers of a court of bankruptcy, where its resources will be gathered in to satisfy the claims of creditors. One of those resources is the liability of the partner, for which his individual property stands charged."[2] All this may be conceded, but it is difficult to see why

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[1] 184 U. S. 18, *supra*, p. 599, n. 2.

[2] The court also relied upon the fact that the non-bankrupt partner was a party to the proceedings. It was necessary to make him a party because each partner is entitled to resist the application to have the firm adjudged bankrupt whether the petition be filed by creditors or by the other partners. But if only the adjudication of the firm is prayed for, no affirmative decree can be made against the partner personally. He is only a party to resist, if he pleases, an adjudication in bankruptcy of the firm. If the bankruptcy of the partner is also prayed for, yet, if upon a hearing he is declared not subject to be declared bankrupt, he is also out of the case as to any relief against him which could not equally be had against any person not a party. A stranger is just as much subject to a summary order, wherever it is competent for the court to make it, as is a party to the case. The power to make such orders does not depend upon the question whether the person to be affected by it is a party. The declaration that the partner is not subject to be made an involuntary bankrupt is practically a dismissal as to him personally. He is thenceforth, if not formally dismissed as an individual, a mere nominal party, continuing in the case only so far as to affect his interests in the disposition of the firm estate, and he is not entitled to a discharge either from firm or from individual debts.

these propositions do not lead to a conclusion directly opposite to that reached by the court. The court does not say that the property of a partner is one of the resources of the partnership, but only that one of its resources is the liability of the partner. If this means that the obligation of the partner runs to the firm, we have the ideal entity theory. But in that case the firm has only a right of action against the partner, which must be enforced by a suit brought by its trustee and not by a summary order. If the court meant that the liability of the partner runs not to the firm but directly to the creditors, but yet is one of the resources of the firm, still this liability is not the same thing as the property of the partner. Speaking in a broad general way, it may be said that the resources of the firm available for the payment of the debts include the personal liability of the partners in addition to the ordinary firm assets. But this particular "resource" can be only a chose in action, running either in favor of the firm for the benefit of its creditors, or directly to its creditors, and in either case enforceable against a non-bankrupt only by action or suit. It is submitted that unless the individual property of the non-bankrupt partners can be treated as the property of the bankrupt firm, the judgments in these cases cannot be sustained, since the Bankrupt Act gives the court the right to possession only of the property of the bankrupt. The summary orders in these cases may also deprive the non-bankrupt partner of rights which are not in conflict with the Bankrupt Act.

The wage-earner or tiller of the soil may have accumulated property in excess of the statutory exemptions and he may owe money to relatives or friends whom it may be to his interest and whom he may wish to prefer to other creditors who are strangers. Whether this desire is meritorious or not, it is one to the gratification of which he is entitled in some states, and as to him it is not forbidden by the Bankrupt Act because he is not subject under that Act to be put into bankruptcy. Yet by the summary order his property may be taken away from him and distributed in a manner contrary to his wishes and to the rights given to him by the laws of his state. The Bankrupt Act declares that these classes of persons shall not be made involuntary bankrupts. Yet by these summary orders they are made worse off than if the Bankrupt Act had not exempted them, for they are subjected to the burdens of bankruptcy without receiving any of its benefits. They are deprived of their property, but are not entitled to a dis-

charge from their debts. It would be mockery to say that if he does not like this dilemma the wage-earner, or tiller of the soil, or one who has not committed an act of bankruptcy, can file a voluntary petition in bankruptcy. A man ought not to be forced into bankruptcy by such an indirect process. He commits no wrong by trying to escape bankruptcy, for there is no legal obligation on an insolvent debtor to file a petition in bankruptcy.[1] It is, of course, desirable that the separate property of all the partners should be administered at the same time with that of the firm, but expediency does not excuse the exercise of powers not granted to the court. Congress might perhaps have enacted that an act of bankruptcy by the firm should be treated as an act of bankruptcy by each of its members, but this would not cover the cases of the classes of persons exempted from the provisions of the Act.

Under an ideally developed entity theory of partnership, the partners would be looked upon as contributories bound in virtue of the partnership relation to contribute to the firm, in case of its insolvency or bankruptcy, enough to make up any deficiency in partnership assets to pay firm debts. The trustee as the representative of the firm in bankruptcy would then be entitled to sue the partners for such contribution. But the enactment by Congress of a provision for adjudication of the firm as bankrupt cannot change the nature of the partner's liability. That is fixed by the laws of the states and remains the same ; namely, an obligation directly to the creditors. It might, however, seem dogmatic to assert that there could not also be, alongside of and in addition to the direct liability to the creditors, another liability to the firm, enforceable in case of the insolvency or bankruptcy of the firm — a liability to contribute to the payment of debts after the exhaustion of the partnership assets, — but no direct authority has been found. In a suit for the dissolution of a partnership and for an accounting it would seem that if the assets were not sufficient to pay the debts, the court should have jurisdiction to order the *pro rata* share which each partner ought to contribute towards the discharge of the unpaid debts to be ascertained and to appoint a receiver to collect the same. Such an order has been upheld by the Court of Appeals of Virginia in Jordan *v.* Miller,[2] and this

[1] Richmond Co. *v.* Allen, 148 Fed. Rep. 657, 660; Wilson *v.* City Bank, 17 Wall. (U. S.) 473.

[2] 75 Va. 442, 454.

doctrine is inferentially supported by the case of May *v.* Pagett,[1] where it was held that an action at law by a receiver of a partnership against a partner to recover a proportional part of the money required to pay firm debts cannot be maintained, when it does not appear that the partnership accounts have been settled or that the receiver does not have in his hands assets of the firm sufficient to pay the firm debts.

It certainly seems narrow and productive of needless litigation for the court in a suit for the dissolution and settlement of an insolvent partnership to limit its activity to the mere distribution of the proceeds of the partnership property, and then to turn the creditors over to other tribunals to recover the balance of their claims from the partners, — resulting, perhaps, in still further suits among the partners themselves if any one should be compelled to pay more than his proper proportion of such balances. The Supreme Court of Indiana, however, has held that the individual liability of a partner is not a liability to the firm and hence not an asset of the firm, and that therefore it was error to order the receiver of the partnership to collect from an assignee for the benefit of creditors of one of the partners the surplus of the separate estate after payment of the individual creditors, and that the firm creditors should be left to make their own proofs separately in the assignment proceedings.[2]

The law of Hungary furnishes an example of a very satisfactory and equitable method by which the partners may be made to contribute to pay the debts. The Commercial Code, Article 88, imposes upon the partners a joint and several liability for partnership obligations. But it is also provided that when the firm has been adjudged bankrupt and when the assets have been converted into money, and the claims of creditors established so that an order of final distribution can be drawn up, a list may be made showing what sum each member of the firm ought to contribute towards the payment of firm debts. If the members refuse to make the payments thus fixed, the bankruptcy court causes notice to be given of a hearing before the commissioner in bankruptcy, who endeavors to bring about an amicable settlement, and, failing in this, prepares a report of the facts necessary for a decree. This report is presented to the court, which renders a decree thereon,

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[1] 2 Pa. Dist. 276.

[2] Wallace *v.* Milligan, 110 Ind. 498.

notice of which is given to the partners. If the partners do not pay, execution is issued against them.[1]

Whether a like result can be obtained in this country without further legislation by Congress, and whether such legislation would be within the power of Congress, are problems the examination of which limitations of time and space at present forbid. But if the liability of the partners is one of the "resources" of the firm,[2] and if "resources" here means assets, the court ought to find little difficulty in directing the trustee of the firm in bankruptcy to ascertain the proportional amount which each partner should contribute to make up a deficiency in other firm assets, and to collect these amounts by suits against any partners who fail to pay after notice or demand.

J. D. Brannan.

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1 Code de Commerce, Loi sur la Faillite, Art. 257–261, French translation by De la Grasserie.

2 Dickas *v.* Barnes, 140 Fed. Rep. 849, 851, *supra*, p. 601.